

# **Auditor's report**

Greater Tubatse Local Municipality

**30 June 2015**

# Report of the auditor-general to the Limpopo provincial legislature and the council on Greater Tubatse Local Municipality

## Report on the financial statements

### Introduction

1. I was engaged to audit the financial statements of the Greater Tubatse Local Municipality set out on pages xx to xx which comprise the statement of financial position as at 30 June 2015, the statements of financial performance, changes in net assets, cash flows and the statement of comparison of budget information with actual information for the year then ended and the notes, comprising a summary of significant accounting policies and other explanatory information.

### Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2014 (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### Basis of disclaimer of opinion

### Accounting framework

4. The financial statements were not prepared in accordance with SA standards of GRAP in all material respects. The following refers:
  - The municipality did not account for prior period errors in terms of GRAP 3 *Accounting policies, changes in estimates and errors*. All prior period errors were accounted for against the comparative statement of financial performance and were not retrospectively restated as required by GRAP 3.

- The comparative amount for employee cost was restated by R8 238 511. This restatement was not disclosed in the prior period restatements note as required by GRAP 3.
- A material subsequent event regarding the proclaimed disestablishment of the municipality and the establishment of a new municipality that amalgamates Tubatse and Fetakgomo municipalities was not disclosed as required by GRAP 14 *Events after the reporting date*.
- The municipality did not adequately disclose the impairment of assets in the financial statements as required by GRAP 21 *Impairment of non-cash generating assets* which requires the municipality to disclose the nature of assets being impaired, the events or circumstances that led to the impairment and the basis used to determine the recoverable amount.
- The municipality did not comply with GRAP 16 *Investment Property* which requires the municipality to disclose the methods and significant assumptions applied by the Municipality in determining the fair value and whether the determination of fair value was supported by the market evidence or other factors.
- The municipality did not comply with GRAP 25 *Employee Benefits* which requires the municipality to disclose the general description of the type of plan used by the municipality.
- The municipality did not comply with GRAP 24, *Presentation of budget information in financial statements* which requires the municipality to disclose the statement of budget comparison on a comparable basis to actual amounts in the financial statements.
- The municipality did not disclose any financial risk exposures as required by GRAP 104 *Financial instruments*.

## **Statement of financial performance**

5. The comparative total for expenditure as per the statement of financial performance stated as R330 284 811 is overstated by R51 800 913 due to casting errors in the financial statements. There is a consequential impact on the comparative net surplus.

## **Statement of changes in net assets**

6. The statement of changes in net assets contains an unreconciled difference of R 42 982 061 as a result of casting errors in the financial statements as well as journals processed directly to retained earnings. Consequently I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the correctness of the statement of changes in net assets as it was impractical to do so.

## **Statement of budget and actual comparison**

7. The statement of budget and actual comparison contains unreconciled differences amounting to R 9 731 846 as a result of incorrect budget amounts reflected in the statement as compared to the budget approved by Council. Additionally, the

explanations for significant variances between actual and budgeted amounts were incorrect. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the correctness of the statement of budget and actual comparison.

## **Property, plant and equipment**

8. The municipality did not recognise all work in progress expenditure in the accounting records in accordance with GRAP 17, Property, Plant and Equipment. I identified work in progress expenditure amounting to R 5 462 601 incurred by the municipality which was not included in the accounting records and financial statements. Consequently, property, plant and equipment stated at R1 342 587 248 in the financial statements is understated there is a consequential impact on depreciation and accumulated surplus for the current year. A municipal building valued at R9 700 000 was incorrectly accounted for as, Investment Property (GRAP 16) instead of Buildings under GRAP 17 Property, Plant and Equipment. This has a consequential impact on the fair value gain and depreciation in the statement of financial performance

## **Receivables from non-exchange transactions**

9. The Municipality made a provision of R17 404 434 (2014: R 39 326 948) for the impairment of receivables from non-exchange transactions as disclosed in note 11 to the financial statements in terms of GRAP 104, Financial Instruments. I was not able to determine the reasonability of the assumptions used in determining this provision as the relevant underlying information supporting the assumptions was not available. I was not able to calculate what the impairment charge against receivables from non-exchange transactions and impairment losses expense should have been had the information been available. Consequently, I was unable to determine whether any adjustments relating to receivables from non-exchange transactions stated at R 92 375 995 (2014: R 55 508 206) in the financial statements and the consequential impact on surplus for the period and accumulated surplus, were necessary.

## **Revenue**

10. I was unable to obtain sufficient appropriate audit evidence that the municipality has correctly billed for all service charges and property rates. The dumping site did not have a weighbridge to enable the charging of dumping levies and the valuation roll was not updated to ensure that all rate payers are billed for refuse collection and property rates. I was unable to confirm the understatement of revenue by alternative means. Consequently, I was unable to determine whether any adjustments to revenue stated at R423 667 368 (2014: R330 284 811) in the financial statements were necessary. Additionally, there is a consequential impact on the receivables from non-exchange transactions.

## **Value added tax (VAT)**

11. I was unable to obtain sufficient appropriate audit evidence for adjustments amounting to R 6 150 071 processed to adjust VAT receivable. I was unable to confirm these adjustments through alternative procedures. Consequently, I was unable to determine whether any adjustment to the VAT receivable stated at R 42 320 (2014: (R 2 308 908)) in the financial statements, was necessary.

## **Payables from exchange transactions**

12. I was unable to obtain sufficient appropriate audit evidence to verify payables from exchange transactions amounting to R 17 848 369 as supporting payables listings could not be availed for audit. Additionally, I identified journals amounting to R5 941 914 that could not be supported. I was unable to confirm the payables from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments to payables from exchange transactions stated at R 52 402 609 (2014: R44 812 754) were necessary.

## **Cash flow statement**

13. SA Standards of GRAP 2 Cash flow statements, requires that the municipality summarises its operating, investing and financing activities. Cash flows from operating activities were understated by R 23 826 668 as a result of the municipality not reflecting the cash flows as per the requirements of GRAP 2.

## **Prior year adjustments**

14. During 2014, I was unable to obtain sufficient appropriate audit evidence for journal entries amounting to R232 592 150 and payment vouchers amounting to R 25 404 817. Consequently, I was unable to determine whether any adjustment to the financial statements was necessary. My audit opinion on the financial statements for the period ended 30 June 2014 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures. I was also unable to obtain supporting documentation for journals posted to accumulated surplus amounting to R37 204 656 in 2015 as internal controls were not established over recording and safekeeping of records. Consequently I was unable to determine whether any adjustments relating to accumulated surplus stated at R1 650 174 473 (2014: R1 634 042 369) in the financial statements was necessary.

## **Commitments**

15. I identified commitments to the amount of R 4 379 181 that were not included in the financial statements. As the municipality did not maintain adequate records for commitments, I was unable to determine the full extent of the understatement in commitments as it was impracticable to do so. Consequently, I was unable to determine whether any adjustment relating to commitments stated at R182 354 037 (2014: R2 481 897) in the notes to the financial statements was necessary.

## **Loans payable**

16. The municipality had outstanding borrowings with a financial institution amounting to R15 910 491 at 30 June 2015. These financing agreements contain certain loan covenants which the municipality must comply with. Failure to comply with the debt covenants may result in the reclassification of the loans to current borrowings in terms of GRAP 1 Presentation of financial statements. The municipality could not provide sufficient appropriate evidence to confirm whether it complied with all the loan covenants. I was unable to confirm compliance by alternative means.

Consequently I was unable to confirm whether the loans have been correctly classified as non-current liabilities.

## **Irregular expenditure**

17. The municipality did not include particulars of irregular expenditure in note 45 to the financial statements as required by section 125(2)(d) of the MFMA. The municipality made payments in contravention of the supply chain management requirements which were not included in irregular expenditure, resulting in irregular expenditure being understated by R8 454 387. The municipality did not have adequate systems in place to identify and report on all irregular expenditure incurred. Consequently I was unable to determine the full extent of the understatement in irregular expenditure as it was impracticable to do so.

## **Disclaimer of opinion**

18. Because of the significance of the matters described in the basis for the disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly I do not express an opinion on the financial statements.

## **Emphasis of matter**

19. I draw attention to the matters below. My opinion is not modified in respect of these matters.

## **Restatement of corresponding figures**

20. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during 2015 in the financial statements of the municipality for the year ended 30 June 2015.

## **Significant uncertainties**

21. With reference to note 39 to the financial statements, the municipality is the defendant in various lawsuits. The ultimate outcome of the matter cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

## **Unauthorised expenditure**

22. As disclosed in note 43 to the financial statements, unauthorised expenditure amounting to R1 423 238 was incurred due to management's failure in planning, budgeting and financial management.

## **Fruitless and wasteful expenditure**

23. As disclosed in note 44 to the financial statements, fruitless and wasteful expenditure to the amount of R1 531 202 was incurred due to interest on late payments.

## **Material under spending of the conditional grants**

24. As disclosed in note 15 to the financial statements, the municipality has materially underspent its conditional grants by an amount of R39 553 395. The under spending

relates to poor planning, human capacity constraints and delays in the tender processes on capital projects. Due to the economic growth point of the municipal area, the developments were mostly performed by the private sector. The allocated grants were not in all instances used, as a consequence the municipality has not achieved its objectives of rendering quality services to the community.

## **Additional matters**

25. I draw attention to the matters below. My opinion is not modified in respect of these matters.

## **Unaudited supplementary schedules**

26. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

## **Unaudited disclosure notes**

27. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

## **Withdrawal from the engagement**

28. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. But for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the ISAs.

## **Report on other legal and regulatory requirements**

29. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

## **Predetermined objectives**

30. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2015:

- Development priority 2: Basic Service Delivery and Infrastructure Development on pages x to x
- Development priority 5: Local Economic Development on pages x to x
- Development priority 5: Spatial Rational on pages x to x

31. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

32. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for managing programme performance information (FMPPI).

33. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

34. The material findings in respect of the selected development priorities are as follows:

### Usefulness of reported performance information

35. I did not identify material findings on the usefulness of the reported performance information for the following development priorities:

- Basic Service Delivery and Infrastructure Development
- Local Economic Development
- Spatial Rational

### Reliability of reported performance information

#### **Development priority: Basic Service Delivery and Infrastructure Development**

36. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Due to inadequate systems I was unable to place reliance on the validity, accuracy and completeness of the reported performance for basic service delivery and infrastructure development. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and differences identified between the reported performance information. The municipality's records did not permit the application of alternative audit procedures.

#### **Development priority: Spatial Rational**

37. The FMPPI requires municipalities to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets.

Significantly important targets were not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures or documented system descriptions for the accurate recording of actual achievements recording and lack of frequent review of the validity of reported achievements against source documentation.

## **Additional matter**

38. I draw attention to the following matters:

### **Achievement of planned targets**

39. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the qualified and disclaimer of conclusions expressed on reliability of the reported performance information in paragraphs xx and xx of this report.

### **Adjustment of material misstatements**

40. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for basic service and infrastructure development, local economic development and spatial rational development priorities. As management subsequently corrected only some of the misstatements, I identified material findings on the reliability of the reported performance information.

## **Compliance with legislation**

41. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

## **Budget**

42. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

## **Annual financial statements, performance and annual report**

43. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not corrected, which resulted in the financial statements receiving a disclaimer of opinion.

44. The annual performance report for the year under review did not include measures taken to improve performance as required by section 46(1)(c) of the MSA.

## **Audit committee**

45. The performance audit committee did not review all the quarterly internal audit reports on performance measurement, as required by Municipal planning and performance management regulation 14(4)(a)(i).
46. The performance audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to Council, as required by Municipal planning and performance management regulation 14(4)(a)(iii).
47. The audit committee did not meet at least four times a year, as required by section 166(4)(b) of the MFMA.
48. The performance audit committee did not meet at least twice during the financial year, as required by Municipal planning and performance management regulation 14(3)(a).

## **Procurement and contract management**

49. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by Supply Chain Management (SCM) policy in contravention of SCM regulation 16(b) and 17(b).
50. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
51. Contracts were extended without tabling the reason for the proposed amendment in the Council of the municipality, as required by section 116(3) of the MFMA.
52. The performance of contractors or providers was not monitored on a monthly basis as required by section 116(2)(b) of the MFMA.
53. Awards were made to providers who are in the service of the municipality in contravention of section 112(j) of the MFMA and SCM regulation 44.
54. Persons in service of the municipality whose close family member had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e).
55. Prospective providers were not invited to apply for listing in the list of approved prospective providers at least once a year as per the requirements of SCM regulation 14(1)(a)(ii) and 14(2).

## **Human resource management and compensation**

56. The senior managers directly accountable to the municipal manager did not sign performance agreements as required by section 57(2)(a) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

## **Expenditure management**

57. Money owing by the municipality was not always paid within 30 days as required by section 65(2)(e) of the MFMA.
58. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made, as required by section 65(2)(b) of the MFMA.
59. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA

## **Consequence management**

60. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

## **Internal control**

61. I considered internal control relevant to my audit of the financial statements, the annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in disclaimer of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

## **Leadership**

62. Oversight responsibility regarding financial and performance reporting and compliance and related internal controls was not exercised as those charged with governance did not investigate unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality in the prior years.
63. There was no detailed review of the financial statements and the annual performance report, resulting in several misstatements not identified and corrected.
64. Municipal officials that deliberately or negligently ignore their duties and disobey legislation were not dealt with through an adequate performance management process as performance evaluations were not done for the year under review.
65. There is a lack of commitment to address deficiencies identified by the auditors as evidenced by many repeat findings. The action plan was not fully implemented and not regularly monitored.

## **Financial and performance management**

66. There is lack of financial reporting skills in the municipality which results in over reliance on the work of consultants.
67. The basic accounting principles of daily and monthly accounting and reconciling have not been implemented.

68. Supply chain management processes were inadequate resulting in irregular expenditure.
69. The financial statements and other information to be included in the annual performance report are not reviewed for accuracy and completeness by the accounting officer.

## **Governance**

70. The internal control monitoring mechanisms of the audit committee and the internal audit are not functioning optimally, as many control weaknesses are only uncovered during the audit of the financial statements and performance information

*Auditor GENERAL*

Polokwane

30 November 2015



*Auditing to build public confidence*